

ISLAMIC REPUBLIC OF PAKISTAN
OCTOBER 2008

CREDIT GUARANTEE COUNTRY PROFILE:

IES/02: ATTACHMENT N

Country Rating	S/T Business Cycle Indicator	S/T Political Indicator	Debt Recovery
3C	→	→	A collection agent is best suited.

Credit Guarantee Experience

Cover in this market is restricted to CILC. The restriction in the cover terms is indicative of the inherent high risk in conducting business with this country. Exporters should as a result exercise extreme caution when dealing with this market and ensure that they have adequately protected themselves against the eventuality of non-payment.

Political Highlights

- ❑ Interim chief of state for August 2008 was Mohammedmian Soomro, following the resignation of former President Pervez Musharraf.
- ❑ A clear majority elected Asif Ali Zardari as president after three provincial assemblies in the country passed resolutions giving him full support in the September presidential election. The husband of the late Benazir Bhutto is seen by some as a corrupt, bullying chancer and by other as a likeable, experienced and sharp-witted middle-aged man. Zardari, who is soon to be elected at president, is not expected to succeed in uniting the 175m fractious Pakistanis.
- ❑ The opposition four-party alliance that came to power after the elections in February will now have to get to grips with its biggest challenges – a possible economic meltdown and the growing militant threat in the north-western tribal areas bordering Afghanistan. If the alliance fails, it could mean the end of the hopes of Pakistan ever becoming a successful democracy. Divisions have already appeared between the parties of the alliance raising doubt over their ability to work with one another.
- ❑ The country's poor security situation remains another important concern. Government's initial efforts to stem the rising tide of Islamist militant attacks seem no more effective than the previous regime of Pervez Musharraf and this may place increasing strain on ties with the US. After announcing that the Inter-Services Intelligence, the military agency, would be brought under civilian control in August, Government reversed the decision within a few hours.
- ❑ Pakistan and the US intelligence agencies claim that the bomb blast on the 20th of September which killed 53 people in the capital was the operation of the al-Qaeda or an affiliate in an attempt to destabilise the country and its democracy.

Recent Economic Highlights

- ❑ Pakistan has a population of 168m with a growth rate of 1.8% expected in 2008.
- ❑ Annual average GDP growth is forecast at 6% in 2008, 4.4% in 2009 and 4.9% in 2010 from 6% in 2007. Growth is expected to be driven by private consumption and investments.
- ❑ The monetary policy committee will remain focused on controlling inflation, which is forecast to average 18.6% in 2008, 11.3% in 2009 and 6% in 2010 from 7.6% in 2007. The EIU believes that Government's efforts to reduce fiscal debt by lowering subsidies on food and fuel, will aggravate inflationary pressure and raised its forecast to average 14.9% from 13.7% for 2008. Inflation reached a thirty-year high of 21.5% in June.
- ❑ Trade deficit soared to \$1.87bn in August due to the week-long action by truck drivers at the port in Karachi that disrupted millions of dollars worth of exports. The import bill for petroleum products rose 66% to \$11.4bn in the twelve months to July, while the food import bill more than doubled to \$4.2bn in 2007-08 from 2006-07. Rising import costs have halved Pakistan's foreign currency reserves from October 2007.
- ❑ Foreign exchange reserves now amount to \$4bn dollars – equivalent to one month's imports. Total forex reserves stand at \$8.89bn, out of which commercial banks have \$3.38bn and the State \$5.5bn. Pakistan is awaiting various injections of about \$7bn from deals with Saudi Arabia and the UAE.



- ❑ The State Bank of Pakistan (SBP) has devised comprehensive guidelines to provide Islamic financing to the agricultural sector. The guidelines are aimed at facilitating Islamic banks and conventional banks involved in agriculture financing and having Islamic banking licences in developing specialized Islamic financing products to meet the financial needs of the farming community. It covers modes of financing that can be used for meeting the financing requirements of farm and non-farm sector activities, including livestock, fisheries, poultry, orchards, etc. Agricultural credit disbursements have increased from Rs39bn in 2000 to Rs212bn in 2008 with the number of Islamic banking branches growing to 313 country-wide.
- ❑ The Pakistan Apparel Forum (PAF) has urged the Government to discourage exports of agri-based products such as cotton and other edibles to ensure their uninterrupted supply to the domestic market. This came after the export of agricultural products showed a tremendous increase in the first month of current fiscal year. The forum feels that measures should be taken to discourage the export of basic raw material to protect the industry. Exports of finished and value-added products of manufacturing sector declined in July, while the export of seeds, rice and cotton has soared 120%. The Federal Minister for Food and Agriculture and Livestock noted that the upliftment of small farmers is paramount to boost the agricultural sector on which the country is heavily reliant. Due to the scarcity of energy resources many industrial units have stopped working and agriculture has become extremely important to the economy.
- ❑ Government's recent decision to increase the power tariff by 31% was met with strong opposition by the Pakistan Industrial and Traders Associations Front (PIAF). The industry is currently undergoing a difficult time and the power price increase would further exacerbate the situation. The Association urged Government to tap into coal reserves instead of continuing with thermal power. The Federation of Pakistan Chambers of Commerce and Industry also reacted strongly to the price increase as electricity charges will ultimately increase the cost of production of the industrial sector. The result will be a negative impact on the textile and cement sectors in particular and eventually on the general economy due to inflation.
- ❑ The Asian Development Bank has endorsed Pakistan's economic policies and announced to support its efforts to overcome the ongoing financial crisis. The ADB has agreed to give \$1.2bn to Pakistan with the first tranche of \$500m being received in the third week of September. Pakistan is facing serious Balance of Payments problems due to unprecedented hike in the oil import bill, which touched \$14bn during the last financial year ended 30th June 2008. The ADB supports the development of infrastructure, public utilities and economic reforms.

Trade Developments

- ❑ Main exports: textiles (garments, bed linen, cotton cloth, yarn), rice, leather goods, sports goods, chemicals, manufacturers, carpets and rugs.
- ❑ Main imports: petroleum, petroleum products, machinery, plastics, transportation equipment, edible oils, paper and paperboard, iron and steel and tea.
- ❑ Major trade partners: US, UAE, Afghanistan, China, UK, Saudi Arabia, Kuwait and Japan.
- ❑ Pakistan and the US will soon finalise an agreement for the import of 50,000 tonnes of wheat on deferred payments by the end of this month. The deal to import the wheat from the US will be followed by working out modalities for subsequent similar agreements to build the domestic wheat stock. A similar agreement with Canada will soon be complete. Government has decided to import 2.5m tonnes of wheat to meet the soaring domestic demand. Pakistan decided to defer payments to avoid depleting its foreign exchange reserves.
- ❑ Pakistan has agreed to provide agricultural land on a large scale to Arab countries including Saudi Arabia and the UAE to build farms to overcome the crisis of food grains. Government held talks with the Saudi Government for obtaining crude oil worth \$6bn on deferred payments in a bid to endure the international price-hikes in crude, while attracting the existing petro-dollars in the Arab world for direct investments in Pakistan.
- ❑ South Korea's Chief of Mission for the Karachi office has confirmed that a Korean shipbuilding company, Hyundai Heavy Industries, was keen to invest in the country and set up a 1.7MW unit to overcome electricity shortages. The unit

can be set up in a container through which around 3.000 homes can be electrified. To overcome Sindh's electricity deficiency, another S Korean company was in talks with local representatives to install a 175MW plant worth \$160m and which will be completed next year. South Korea is also interested in importing textile products from Pakistan. There are about 200 South Korean businessmen living in Pakistan and 25 companies operating there.

- Pakistan and Bangladesh have agreed to review the existing shipping agreement between them as efforts to increase the trade volume through improved shipping will benefit both countries. Pakistan's Government was committed to foster close cooperations with Bangladesh given their close proximity and understanding on bilateral and regional issues.
- South African exports to Pakistan totaled R1.02bn in 2005, R1.08bn in 2006, R1.5bn in 2007 and R439m in the year to March 2008.

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